Global Digital Taxes and Minimum Taxes are Upon Us

Background

The Organisation for Economic Co-operation (OECD) is meeting this week to discuss its extraordinary undertaking to gain consensus among 137 member states to adopt a global regime for taxation of businesses conducted through digital means ("digital taxes") and global corporate minimum taxes. As ambitious as this undertaking may seem, indications are that at least some form of multilateral tax regime, whether under the auspices of the OECD or the European Union (EU), will emerge from these efforts as early as 2021. If adopted, this would have a potentially transformational impact on the conduct of not just tech businesses but multinational businesses in general.

COVID-19 Impact

Efforts have been underway for some time to reform the approach to multijurisdictional taxation but progress has been slow or in many cases non-existing. However, the COVID-19 pandemic, which has created a boom for digital commerce in general and given rise enormous needs for governments to raise tax revenues, has brought these efforts to the forefront of tax policy makers around the world. A digital tax is perceived by the OECD and the EU as well as many NGOs and governments around the world as a fundamental component to funding the global recovery from the COVID-19 pandemic. The EU has committed EUR 750 billion to help member states rebound from the pandemic, and it is envisioned that a digital tax will be crucial and necessary to pay for those contributions.

What is Involved?

The stated objective of the digital tax initiatives is to meet the tax challenges created by the digitalization of the global economy. Stated differently, the idea is to make multinational companies in general, and "big-tech companies" in particular, pay significantly greater taxes. It is argued that the digitalization of businesses has allowed large companies to escape taxation by operating beyond traditional tax jurisdictions. Many countries who consider themselves "market jurisdictions" (i.e., where the customers or "users" of digital services are located) take the position that they should have the ability to tax digital revenue derived in their jurisdictions. However, the contemplated OECD tax regimes go well beyond that objective. If adopted, most companies that operate internationally, whether in tech or non-tech areas, or a combination thereof, will be affected. Indeed, the OECD has announced that it will propose a form of global minimum tax that would cut across all industries and businesses.

What Are the Odds This Will Materialize ?

Many countries have already adopted various forms of unilateral digital taxes. Both the OECD and the EU are working on parallel tracks to adopt multilateral rules that would mandate the adoption of digital taxes among member states, and, it is hoped, that would harmonize rules among the different states. Many NGOs have weighed in support of these projects and even the UN has gotten involved. However, the digital tax efforts have been met with opposition from several sources including, perhaps not surprisingly, countries that perceive that they may have to concede tax jurisdiction to the market jurisdictions, including the U.S., as well as several industry organizations.

The OECD has repeatedly stated that the digital tax system must be adopted as early as 2021, but recently conceded that there may not be agreement on the new rules until 2021. It should be noted that the adoption of the OECD proposal would require unanimous agreement by all 137 countries that are involved in the project. Separately, EU Commission President Ursula von der Leyen has repeatedly indicated that, barring the adoption of the OECD proposal by 2021, the EU will implement its own rules in 2021. As indicated, the EU has committed EUR 750 billion as COVID-19 recovery aid to member states and the digital tax is a critical component in funding that cost. Thus, despite opposition and threats of trade barriers, indications are that we will see some form of multilateral digital tax regime adopted in 2021.

OECD Proposal

Description

Remarkably little detail is available regarding the OECD proposal (referred to as the "Inclusive Framework") given that we are less than two months away from the envisioned effective date of the new regime. It is anticipated that more information will emerge following the OECD meetings this week.

While details are scant, the OECD proposal consists of two components ("Pillar I" and "Pillar II") having the following characteristics:

I. Pillar I would grant tax jurisdiction over certain digital services income to the "market jurisdiction" (generally, the jurisdiction where the users are located). There are two types of taxable profit that may be allocated to market jurisdictions: "Amount A" –a deemed "residual" profit amount remaining after allocating profits attributable to activities conducted in other countries; and "Amount B" – a fixed remuneration amount for marketing and distribution. Amount A is limited to income from certain types of businesses that meet the relevant nexus rules including automated digital services, online search engines, social media platforms, online intermediation platforms (e.g., marketplaces), digital content streaming, online gaming, online advertising, and cloud computing. Amount A income may not include income from business platforms with a high degree of human judgment such as services for legal, accounting, consulting, etc. or "consumer-facing" businesses.

II. Pillar II would impose additional taxes on multinational businesses that do not meet certain benchmark requirements with respect to global tax payments. It is generally presently unclear how these benchmarks would be designed or how the minimum tax collections would be allocated among the various jurisdictions.

Adoption/Implementation

The implementation of the OECD proposal would require unanimous agreement among all 137 countries who have adopted the Inclusive Framework. If enacted, each country would adopt implementing national legislation.

Timing

The OECD has repeatedly indicated that the new rules will come into effect in 2021. However, the negotiations among the OECD members have not progressed as fast as envisioned. The head of OECD tax policy, Pascal Saint-Amans, recently indicated that he did not expect a consensus agreement on the proposal until 2021. Nevertheless, thus far the OECD has not backed off the goal to bring the new rules into effect by 2021.

Comment: It is unclear how the OECD proposal would be implemented in light of the extensive network of tax treaties in existence among the OECD members and other countries. Those treaties, many of which are based on the OECD model convention, contain provisions that may be inconsistent with the intended scope of the digital tax and minimum tax proposals.

EU Proposal

Description

In general, the EU position is that digital taxation needs to be addressed with an interim, temporary solution accompanied by a long-term, permanent fix. Many EU member states have already adopted or are in the process of adopting digital taxes and the EU Commission has indicated that the rationale for a unified EU proposal is to mitigate the risk of fragmentation of the single market by the adoption of unilateral digital tax rules among the member states.

The EU Commission made a proposal labeled "fair taxation of the digital economy" on 21 March 2018. The proposal consists of an interim component and a long-term component, which can be summarized as follows:

- The "interim proposal" is to introduce a tax imposed at 3% on gross revenues derived from certain "digital services," such tax referred to as a "digital services tax" or "DST." Digital services include the sale of online advertising space, acting as digital intermediary/facilitator of online sales, and the sale of data generated by users. The interim DST would apply only to enterprises operating above two thresholds: 1. with total annual worldwide revenues above EUR 750 million, and 2. total annual EU revenues exceeding EUR 50 million. The interim tax would apply equally to EU resident and EU non-resident companies, and would apply to both domestic and cross-border transactions. The digital services tax would be adopted at the national level by each EU member state and would allow each member state to levy tax on gross receipts based on the number of "users" of the digital service in each member state.

- The "long-term solution" involves a regime under which any company, regardless of physical presence, that has a "significant digital presence" in an EU member state would be treated as conducting a taxable business operation in the state and would be taxed in a manner similar to a regular "bricks and mortar" company. A company would be considered to have a significant digital presence if it has annual digital service revenues exceeding EUR 7 million, over 100,000 users in a member state, or more than 3,000 business-to-business contracts for digital services performed by the company. The amount of DST that could be levied by each member state would be based on a proportionate allocation of profits among the member states. The tax rate would be equivalent to tax imposed on "bricks and mortar" businesses. The tax would cover not only corporate taxpayers incorporated or established in the EU, but also those incorporated or established in a non-EU jurisdiction. The proposal contemplates that the concept of "significant digital presence" may be negotiated and defined in tax treaties between EU member states and non-EU member states.

Adoption/Implementation

Each member state would adopt a national DST that implements the proposed EU directive. The adoption by the EU of a tax directive generally require unanimous agreement by the member states. The European Parliament has expressed support for the DST but does not have the power to force the adoption of the tax. It is presently unclear whether the EU Commission has unanimous support among the EU members for the DST proposal.

Timing

EU Commission President Ursula von der Leyen stated on 16 September 2020 that the EU is committed to supporting the OECD's work but the EU will propose a digital tax in early 2021 if the global OECD effort has not been adopted by then.

According to the EU lawmakers, revenues from an EU digital tax should be paid into the EU budget beginning in 2023.

Comment: Germany holds the rotating presidency of the Council of the EU from July to December 2020, meaning it chairs meetings and represents the EU in international negotiations. Germany currently does not have plans to implement a DST but has indicated support for the OECD initiative.

U.S. Position

It is no secret that the U.S.-based "big-tech companies" are intended targets of the digital tax proposals. It has been stated that the big-tech companies are able to escape taxation by having a digital, as opposed to a physical, presence in various markets, and therefore do not pay an adequate amount of taxes.

The U.S. Treasury Department has indicated that it is generally opposed to the current digital and global minimum tax proposals which the Treasury Department considers discriminatory to U.S. big-tech. The Treasury Department believes that the EUR 750 million revenue threshold adopted in several digital tax proposals, including the EU proposal, is directly aimed at U.S. big-tech companies by effectively exempting many tech companies other than the U.S.-based big-tech companies from the digital tax.

France, an early adopter of a digital tax, has enacted a digital tax that imposes a digital tax only on companies that have revenues in excess of EUR 750 million, a criterion very few non-U.S.-based tech companies would satisfy. French tax policy makers have made public statements to the effect that the digital tax was aimed specifically at U.S. big tech. The EUR 750 million threshold has been adopted by the EU as well as several national digital tax regimes.

In June 2020, the U.S. Treasury Department communicated that multilateral negotiations on digital taxes under the auspices of the OECD had reached an impasse. The U.S. Treasury Department later clarified that it intended to pause negotiations in order to permit focus on economic matters related to COVID-19. The U.S. has indicated that it is seeking a broader application of the Pillar I taxes on digital services with the possibility of a safe harbor for those taxpayers that meet tax obligations under currently applicable tax regimes. The French Minister of Economy and Finance called the U.S. move a "provocation." The U.S. has signaled more flexibility to continue negotiations on Pillar II taxes, those aimed at setting a minimum tax on global income, provided that the

U.S. tax on Global Intangible Low Taxed Income ("GILTI"), enacted under the Tax Cut and Jobs Act in 2017, would count for these purposes. The U.S. position is also that Pillar II should not be confined to the tech sector, but should apply to all "customer-facing" businesses.

The U.S. and the OECD are still in discussions concerning Pillars I and II. Recent indications suggest that the OECD may offer an exemption from Pillar II for companies that are subject to the U.S. GILTI tax - that is, the GILTI tax would be treated as an implementation of Pillar II, which would effectively exempt U.S. companies from Pillar II. If adopted, that would presumably go a long way towards appeasing the U.S. opposition to Pillar II.

In addition, the U.S. Treasury Department recently announced that it would not consider digital taxes imposed without regard to nexus in a particular jurisdiction as qualifying for foreign tax credits for U.S. tax purposes. What this means is that the U.S. would not concede tax jurisdiction to the digital taxation countries with respect to digital revenues. The U.S. Treasury Department indicated that it might modify its position on this topic based on negotiations with the OECD.

Trade

France was early out the gate to introduce a digital tax. The U.S. opposed the French digital tax and threatened France with trade sanctions. The French government eventually backed down, indicating that it would suspend collection of the tax until 2021 and engage in bilateral and multilateral negotiations to resolve the dispute.

In June 2020, the U.S. Trade Representative initiated investigations pursuant to Section 301 of the Trade Act of 1974 on several jurisdictions including: Austria, Brazil, the Czech Republic, the European Union, India, Indonesia, Italy, Spain, Turkey, and the United Kingdom. The investigations are the U.S. response to the enactment or proposed enactment of unilateral digital services taxes in such counties. The U.S. could impose punitive tariffs on goods from any jurisdiction found to be subject to Section 301. The U.S. views the application of digital taxes on large tech companies as discriminatory taxes levied on U.S. companies potentially amounting to tariffs.

Trump vs. Biden

The U.S. position on digital tax and global minimum tax has been articulated by the Trump Administration. There has only been speculation about the approach of a Biden Administration in the event of a Biden win in the November presidential election, as there has been no indication from the Biden camp as to how it would approach the OECD and EU proposals.

Unilateral Digital Tax Initiatives

In the absence of immediate measures on digital taxation by the OECD or the EU, several states have adopted or announced that they will adopt digital tax regimes. Many of the national taxes have features in common with the EU Commission proposal. Set forth below are general descriptions of a sample of digital tax regimes adopted or proposed in various jurisdictions.

Digital Taxes Adopted

European Union – Digital Services Taxes on member state level (selection of already enacted DST)

- **Austria:**

Effective Date:	1 January 2020
Rate:	5%
Taxable Persons and Applicable Tax Base:	The digital tax applies to companies with global turnover of EUR 750 million or more, and a national turnover of at least EUR 25 million from online advertising services. Revenues from advertising services on digital interfaces or any type of software or websites rendered in Austria.

- **France:**

Effective Date:	1 January 2019 but 2020 DST collection has been delayed to the end of 2020
Rate:	3%
Taxable Persons and Applicable Tax Base:	The digital tax applies to companies with global digital turnover of more than EUR 750 million and digital turnover of more than EUR 25 million in France. The digital tax is generally imposed on the French portion of "digital service receipts" which is determined based on French digital presence, i.e., the ratio of French digital services receipts to worldwide digital services receipts. Digital services receipts generally include: 1. Provision of a digital interface enabling users to enter into contacts and to interact with others ("intermediary services");

	and 2. The provision of services to advertisers that aim at placing targeted advertising messages on a digital interface based on data collected about users and generated upon the consultation of such interface ("advertising services based on users' data").
Sunset Clause:	The French DST will be withdrawn/replaced once measures agreed at international level to tax the digital economy will enter into effect.

- **Italy:**

Effective Date:	1 January 2020
Payment Date:	16 February of the following year (e.g., 2020 due 16 February 2021)
Taxable Persons:	Resident and non-resident entities which meet the following conditions in the previous calendar year: 1. total amount of worldwide revenues of more than EUR 750 million; and 2. total amount of revenues deriving from digital services provided to users located in Italy is more than EUR 5.5 million.
Rate:	3%
Applicable Tax Base:	Revenues (gross of costs and net of VAT and other indirect taxes) deriving from digital services provided to users located in Italy. Digital services include: 1. Advertising on a digital interface; 2. A multilateral digital interface that allows users to buy/sell goods and services; and 3. The transmission of user data generated from using a digital interface. A user is deemed to be located in Italy based on different criteria. The criteria generally make reference to the user's device location which, in its turn, is identified by making reference to the internet protocol address of the device or to any other method of geo-localization. When a taxable service is supplied in Italy in a calendar year

	the taxable revenue is the percentage of worldwide revenue from digital services that is represented by the services linked to Italy. The determination of the percentage varies based on the category of digital service.
Sunset Clause:	The Italian DST will be withdrawn/replaced once measures agreed at international level to tax the digital economy will enter into effect.

- **United Kingdom:**

Effective Date:	1 April 2020
Rate:	2%
Taxable Persons and Applicable Tax Base:	The U.K. digital tax generally applies to companies with global digital turnover of more than £ 500 million and digital turnover of more than £ 25 million in UK. The digital tax is generally imposed on revenue derived from three types of digital activities: 1. social media platforms; 2. internet search engines; and 3. online marketplaces.

- **Poland:**

Effective Date:	1 July 2020
Rate:	1.5%
Applicable Tax Base:	Gross revenue from: 1. access to audio-visual media service; and 2. audio-visual commercial communication.

Digital Tax Proposed or Considered (selection)

- **Belgium:**

Effective Date:	TBD
Status:	Proposed
Rate:	3%
Taxable Persons and Applicable	The tax would apply to companies with global turnover of EUR 750 million or more, and a national turnover from

Tax Base:	digital activities of at least EUR 5 million. Revenue subject to the digital tax include revenue from the following sources: 1. The sale of advertising space on a digital platform targeted at its users; 2. The sale of user data generated from user activities on a digital platform; and 3. The provision of digital intermediation services to users of a digital platform by facilitating the exchange of supplies of goods or services between those users.

- **Canada:**

Effective Date:	TBD
Status:	Intention
Rate:	3%
Taxable Persons and Applicable Tax Base:	The tax would apply to companies with more than C$1 billion in worldwide revenue and Canadian digital revenue of more than C$40 million. Similar to the French DST, taxable revenue includes revenue derived from: 1. The provision of a digital interface enabling users to enter into contacts and to interact with others ("intermediary services"); and 2. The provision of advertising services based on users' data.

- **Czech Republic:**

Effective Date:	TBD
Status:	Proposed
Rate:	5%
Taxable Persons and Applicable Tax Base:	The tax would apply to companies with global turnover of EUR 750 million or more, and a digital turnover of at least CZK 100 million (US$4 million) in Czech Republic. Taxable revenues include revenue from the following sources: 1. targeted advertising on a digital interface;

	2. the transmission of data about users and generated from users' activities on digital interfaces; and 3. the provision to users of a multi-sided digital interface which facilitates the provision of supplies of goods and services among users.

- **Spain:**

Effective Date:	TBD
Status:	Proposed
Rate:	3%
Taxable Persons and Applicable Tax Base:	The tax would apply to companies with global turnover of EUR 750 million or more, and a national turnover of at least EUR 3 million from digital activities. Taxable revenues include revenue from online advertising services, the sale of online advertising and the sale of user-data.

For more information about Curtis, please visit www.curtis.com.

Attorney advertising. The material contained in this Client Alert is only a general review of the subjects covered and does not constitute legal advice. No legal or business decision should be based on its contents.

Please feel free to contact any of the persons listed below if you have any questions on this important development:

Klas Holm
Partner, Global Tax Co-Chair
kholm@curtis.com
New York: +1 212 696 8800

Eduardo A. Cukier
Partner
ecukier@curtis.com
New York: +1 212 696 6107

Olga R. Beloded
Partner
obeloded@curtis.com
New York: +1 212 697 1559

Marco A. Blanco
Partner, Global Tax Co-Chair,
Geneva Managing Partner
mblanco@curtis.com
New York: +1 212 696 6128
Geneva: +41 22 718 3518
Paris: +1 917 368 8828

Martin Wolff
Associate
mwolff@curtis.com
Frankfurt: +49 69 247 576 000

Christian Fingerhut
Partner
cfingerhut@curtis.com
Frankfurt: +49 69 247 576 000

Esther Zuckerman
Associate
ezuckerman@curtis.com
New York: +1 212 696 8862

Francesca Orlando
Counsel
forlando@curtis.com
Milan: +39 02 7623 2028
Rome: +39 06 6758 2201